

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B2

PLR-112800-09

Date: September 2, 2009

X =

State =

\$m =

\$n =

Date1 =

Date2 =

Date3 =

Date4 =

Date5 =

Year1 =

Year2 =

Year3 =

Dear

This responds to a letter dated February 27, 2009, and subsequent correspondence submitted on behalf of X by X's authorized representative, requesting inadvertent termination relief under § 1362(f) of the Internal Revenue Code.

The information submitted states that X was incorporated under the laws of State on Date1 and elected to be an S corporation effective Date2. X had earnings and profits of \$m at the close of Year 1, Year 2, and Year 3 taxable years and had gross receipts for each of those years of which more than 25 percent were passive investment income. As a result, X's S election terminated on Date3. A dividend of \$m was paid Date4.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and not motivated by tax avoidance. X further represents that X has filed returns consistent with X's status as an S corporation. X and its shareholders have agreed to make such adjustments (consistent with the treatment of X as an S corporation) as may be required by the Secretary.

Section 1361(a)(1) defines an "S corporation" as a small business corporation for which an election under 1362(a) is in effect for the taxable year.

Section 1362(d)(3)(A)(i) provides that an election under 1362(a) shall be terminated whenever the corporation has accumulated earnings and profits at the close of each of three consecutive taxable years, and has gross receipts for each of such years more than 25 percent are passive investment income. Section 1362(d)(3)(A)(ii) provides that any termination under 1362(d)(3) shall be effective on and after the first day of the first taxable year beginning after the third consecutive taxable year referred to in 1362(d)(3)(A)(i).

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation (A) was not effective for the taxable year for which it was made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, or (B) was terminated under § 1362(d)(2) or (3), (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent, (3) no later than a reasonable period of time after discovery of the event resulting in the ineffectiveness or termination, steps were taken (A) so that the corporation is a small business corporation, or (B) to acquire the required shareholder consents, and (4) the corporation, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness or termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Section 1375 imposes a tax on the income of an S corporation that has accumulated earnings and profits at the close of a taxable year, and that has gross receipts more than 25 percent of which are passive income (within the meaning of 1362(d)(3)).

Based solely on the facts submitted and the representations made, we conclude that X's S corporation election terminated on Date3 under 1362(d)(3)(A) because X had earnings and profits at the close of each of three consecutive taxable years, and had gross receipts for each of those taxable years more than 25 percent of which were passive investment income. We also conclude that this termination of X's S election on Date3 was an inadvertent termination within the meaning of § 1362(f).

Therefore, we conclude that X will continue to be treated as an S corporation beginning Date3 provided that X's S corporation election was valid until it otherwise terminated under § 1362(d), and provided that the following condition is met. As an adjustment under § 1362(f)(4), a payment of \$n and a copy of this letter must be sent to the following address: Internal Revenue Service, Cincinnati Service Center, 201 West Rivercenter Blvd., Covington KY 41011, Stop 31, Terri Lackey, Manual Deposit. This payment must be sent no later than Date5.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under any other provision of the Code. Specifically, no opinion is expressed regarding X's eligibility to be an S corporation or the validity of its S corporation election. Further, no opinion is expressed as to whether X's income was passive investment income under § 1362(d)(3)(C).

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to a power of attorney on file with this office, a copy of this letter is being sent to X's authorized representative.

Sincerely,

Bradford R. Poston
Senior Counsel, Branch 2
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes